

Interest Calculations February 2001

Recently the PECFA program started to see more claims being submitted where interest reimbursement is controlled by the lower caps that were established in the last state budget bill. These caps limited reimbursement of interest costs to either 1% under prime or 4% depending on gross revenues. Until recently, the claims that we were receiving were still being funded by loans that predated the statutory change and continued to have eligibility at the higher original reimbursement levels.

As time has continued, however, we have transitioned from the era of the earlier loans to the point in time where the common claim submittal will be reimbursed at the lower statutory rates. As part of this transition, we want to highlight to claimants and their lenders a couple of points regarding the interest reimbursement process.

As many loans will be written and charged at interest rates higher than the level that will be reimbursed by PECFA, there needs to be a calculation of interest costs, as part of the claim submittal, that provides the interest charges that are eligible under the fund. This conversion is necessary to identify the share of total interest costs that equal either the allowed prime minus 1% or 4% rate. The factoring process will involve calculating interest charges, minus origination fees and renewal fees, at the 1% under prime or 4% level.

Certainly, the best alternative is for a claim submittal to include the detail and source records of this calculation when it is sent to the department. What we have seen, however, are submittals that claim interest charges at the actual loan rate, which is above the statutory maximum. The PECFA staff can not independently complete the required calculations because they do not have the original source records to construct a fully detailed loan history. Consequently, PECFA must obtain from the lender a calculation of interest costs at the allowed reimbursement rate. The information provided by the lender and verified by PECFA must be the basis for the reimbursement of the claim.

As the program has started to request these calculations, however, we have found that there may be some confusion. The request is not an attempt to induce the lender to forgive interest or to reduce the rate that was charged on the loan. The request is only to solicit the amount that can be legally reimbursed by the fund. Although PECFA may have been provided the total lender charges, the program can not simply take the total lending cost and factor it down to a reimbursement amount. There is frequently no way to independently separate out interest costs, origination fees and renewal charges.

In addition to not having the source documentation to create a reimbursable interest amount, from an audit control standpoint, PECFA staff can not be in the position of independently creating costs for inclusion in an applicant's claim. Such a process would violate basic audit control provisions and move staff from the role of reviewers to one where they would be the originators of claim costs.

We recently ran into an occasion where we were unable to obtain the information necessary to determine the interest reimbursement amount. Because we were not able to obtain a calculation,

we were put in the position having to deny all the interest costs in the claim. Ultimately this issue may be resolved in the appeal process, the delay, however, creates a burden on the claimant and potential additional unreimbursable costs. We realize that the calculation of the interest cost is an additional workload for lenders, but it is a step that is necessary to complete the reimbursement of a claim. With a better understanding of the issue and the reasons behind the need for the calculation, we hope to be able to avoid situations like the one we recently encountered.